No. 2652

In the United States Circuit Court of Appeals

For the Ninth Circuit

A. R. TITLOW, as Receiver of the UNITED STATES NATIONAL BANK of Centralia, Washington,

Appellant,

vs.

JOHN E. SUNDQUIST, WALTER GUSTAFSON and IZELLA J. SMITH,

Appellees.

PETITION FOR REHEARING

UPON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF WASHINGTON, SOUTHERN DIVISION.

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The amount involved in this suit is small. The facts are simple.

The legal principle is important.

You have declared a trust against an insolvent estate on the admitted facts that there was (a) no trust *res,* and (b) no augmentation of the estate.

You rest this decision on *Montagu vs. The Bank,* 81 Fed. 602. The facts in the Montagu case *are not similar.*

In the case at bar the *fact is no new money was deposited in the bank.* It owed Sundquist $3,000. He withdrew part of this in cash and took a new evidence of indebtedness for the balance. There was no deposit of money by Sundquist or any one else. Your Honors have stated the facts concisely, but you have *commented* upon these facts as follows:

"Manifestly the $1296 *left* by Sundquist with the bank, of which the appellant is receiver, to be paid over to Mrs. Smith upon her cancellation of the note and mortgage, executed by her to Gustafson, was not of the latter character, but, on the contrary, was *deposited* with the bank for that specific purpose."

This statement, we believe, is not justified by the facts.

In the Montagu case there was a *deposit of actual funds. There was an augmentation of assets that passed to the receiver.* Let us see.

On June 21st London deposited $5000 in New York to the credit of San Francisco, with instruction to San Francisco to remit it to Seattle. On June 22 San Francisco failed, not having made the remittance. *It was admitted* that the $5000 *deposited and actually*

paid in New York had not been used in balancing accounts, but *was owing to the receiver of San Francisco. What was the trust res? What was the augmentation?* It was the *claim* that the *receiver of San Francisco* had *against* New York, to-wit, $5000. When the San Francisco receiver collected the $5000, there was an augmentation of assets of the insolvent San Francisco bank to that extent. This Montagu case is explained in 11 Harvard Law Review, 202:

"The decision is sound but the reasoning is erroneous, arising from a misconception of the trust *res.* The specific deposit lost its identity as a *res* by being mixed with the funds of the bank of deposit (New York) but as soon as C. (San Francisco) was credited with the amount by the bank of deposit, the former had a claim as a creditor—a common law claim—against the latter. This claim was not extinguished by any actual payment, because as the report expressly states, no funds were transmitted from B. to C. (New York to San Francisco). Nor does it appear from the facts that it was extinguished by any settlement on the books of the bank. The brief interval between the date of deposit and the failure and the general custom of banking would be quite conclusive that there was no such settlement. This unsatisfied claim would be held in trust for the depositor, who did not affect it by any subsequent withdrawals against it. The form of a trust *res* may change and the trust relation remain or a new trust *res* may come into existence during the course of events. The failure to distinguish its form and changes has caused great confusion in the cases. A similar correct result but similar confusion of reasoning characterizes the case of *Farley vs. Turner,* 26 Law J. Ch. 710, cited in the principal case

as directly in point. The foregoing reasoning avoids resort to the authority of cases where the assets of a bank are swollen by the intermixture of trust funds, many of which are cited in the principal case."

In the *Montagu* case let us suppose that *after* the crediting by New York for San Francisco and *after* the failure of San Francisco and before any actual payment by New York to San Francisco, New York had also failed and had paid 50 cents on the dollar. Would Your Honors have held that the complainant was entitled to a preferred claim of $5000 or $2500? Clearly the complainant could only receive as a preferred claim the *amount that the San Francisco receiver obtained from New York.*

This distinction of reasoning is clearly expressed in *Commercial National Bank vs. Armstrong,* 148 U. S. 50.

In that case a Cincinnati bank was acting as agent for a Philadelphia bank in the collection of various items. While this agency relation existed the Cincinnati bank failed and various phases of these collections were presented. The Cincinnati bank had sent some of these collection items to its correspondent banks. In some instances the correspondent bank had collected and credited *but not remitted* to the Cincinnati bank *before its failure.* Remittance was made

to the Cincinnati bank's receiver *after* its insolvency. In that class of cases the court held that the receiver was a trustee of the *claim against the subagent.* The Court said:

"It (the Cincinnati bank) had not fully performed its duties as agent and collector. It had *not received the moneys collected by its subagents as separate and specific funds, and therefore the plaintiff was entitled to have them paid out of the assets in the hands of the receiver, for when he collected them from these subagents, he was in fact collecting them as agent of the principal.*"

Where the Cincinnati bank had made the collection *before* insolvency no preferred claim was allowed.

The Supreme Court had in mind the language in the *Marine Bank* case and quotes the very passage that Your Honors have quoted in the *Sundquist* case.

Your Honors state that it is unnecessary to again cite the authorities relied upon by this Court in the *Montagu* case. Let us examine them. The first is *Peak vs. Elliott,* 30 Kas. 156. Judge Gilbert, in *Spokane County vs. First National,* 68 Fed. 979, quoted from the *Peak* case and stated that it among others laid down a doctrine to which *this Court was unable to give assent.*

The same Court that decided the *Peak* case later repudiated it.

Kansas State Bank vs. First National Bank, 62 Kas. 788, 64 Pac. 634, in speaking of the *Peak* case, the Court said:

"In that case the matter of identifying and tracing the trust fund received but little attention";
and after citing the earlier Kansas cases the Court continued:

"In some of the cited cases the doctrine of the impressibility of insolvent estates with trusts was carried to the full length, and language is used which taken apart from the facts of the case might give countenance to the rule that if the trust fund had been used by the trustee even in payment of his general indebtedness and without increasing the estate which passed to his assignee, it would be sufficient to charge the whole estate with the trust."

The Kansas Court concluded that:

"If the estate had not been *increased by specific additions to it or if what previously existed had not been improved or rendered more valuable, it has not been impressed with the trust claimed.*"

The cases of *Massey vs. Fisher,* 62 Fed. 958, *Anderson vs. Pacific Bank,* 112 Cal. 598, and *Farley vs. Turner,* 26 Law J. Ch. 710, were all similar. In each case *there was an augmentation of assets* In the first, "Massey thereupon gave the cashier *$1225 in*

bank bills." This money "was put into the drawer with the other money of the bank."

In the *Anderson* case:

"To protect defendant and the sureties it might furnish from liability or loss, plaintiff agreed to deposit with defendant *the sum of $2,000 in gold coin as a pledge.* Plaintiff *delivered the money* to McDonald, the acting president of the bank."

In the *Farley* case, your Honors, stating the facts (81 Fed. 607), say that Farley *paid in a further sum of 707 pounds.* In all three of these cases there was *an actual deposit of money over the counter of the bank.* All three of the cases have been subjected to criticism on the ground (a) that the relation between the parties was that of debtor and creditor, and (b) that the fund had not been traced. It must be conceded that in each of the three above cases, there was an actual fund created. There was no fund created in the *Sundquist* case.

An excellent review and explanation of these cases is found in *In re Marsh,* 116 Fed. 396.

The remaining case of *People vs. City Bank of Rochester,* 96 N. Y. 32, supports your Honors' ruling. We believe it is the only case that can be cited in support of the case at bar. The New York court later said

in the matter of *Cavin vs. Gleason,* 105 N. Y. 256, at page 263:

"The case of *People vs. City Bank of Rochester* seems to have been misunderstood. The question considered in this case was not raised there. It was not claimed in that case that the proceeds of the checks of Sartwell, Hough & Co., the petitioners, had not gone into the general funds of the bank or that they had not passed in some form to the receiver. The court did not decide that petitioners would have been entitled to a preference in case the proceeds of the check had been used by the bank and were not represented in its assets in the hands of the receiver."

If your Honors will mark the clear distinction between the mere *shifting of credits* from one form to another and the actual augmentation by the *payment of gold coin over the counter* of the bank, we believe that you will deny the preference in this case to *Sundquist,* which ruling will harmonize with the universal holdings of the Federal courts.

Respectfully submitted,

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Attorneys for Appellant.

This is to certify that I am one of the counsel for the appellant in this case. In my judgment the foregoing petition for rehearing is well founded. It is not interposed for delay.

R. P. Oldham